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**JUL 15 1940**

**CHARLES ELMORE CROPLEY**  
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**IN THE**  
**Supreme Court of the United States**

**OCTOBER TERM, 1940**

**NO. .... 242-243**

**IN THE MATTER OF THE REORGANIZATION OF PITTSBURGH  
RAILWAYS COMPANY, a Corporation, Debtor, and PITTSBURGH  
MOTOR COACH COMPANY, a Corporation, Subsidiary.**

**PHILADELPHIA COMPANY and Certain Underliers, Petitioners,**

**v.**

**WALTER L. DIPPLE, JAMES P. McARDLE, BEN PAUL BRASLEY  
and THOMAS J. HOFFMAN, a Committee Known as the Tort  
Creditors' Committee, and CITY OF PITTSBURGH, Respondents.**

**PETITION FOR WRITS OF CERTIORARI TO THE  
UNITED STATES CIRCUIT COURT OF APPEALS  
FOR THE THIRD CIRCUIT.**

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IN THE  
**Supreme Court of the United States**

**OCTOBER TERM, 1940**

**NO.....**

**IN THE MATTER OF THE REORGANIZATION OF PITTSBURGH  
RAILWAYS COMPANY, a Corporation, Debtor, and PITTSBURGH  
MOTOR COACH COMPANY, a Corporation, Subsidiary.**

**PHILADELPHIA COMPANY and Certain Underliers, Petitioners,**

**v.**

**WALTER L. DIPPLE, JAMES P. McARDLE, BEN PAUL BRASLEY  
and THOMAS J. HOFFMAN, a Committee Known as the Tort  
Creditors' Committee, and CITY OF PITTSBURGH, Respondents.**

**PETITION FOR WRITS OF CERTIORARI TO THE  
UNITED STATES CIRCUIT COURT OF APPEALS  
FOR THE THIRD CIRCUIT.**

*To the Honorable Chief Justice of the United States  
and Associate Justices of the Supreme Court of the  
United States:*

The undersigned, on behalf of Philadelphia Company, owner of all of the capital stock and principal creditor of the above named debtor, and on behalf of certain underliers listed below,\* as petitioners, pray that

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\* Allegheny, Bellevue and Perrysville Railway Company; The Allenport and Roscoe Electric Street Railway Company; Ben Avon and Emsworth Street Railway Company; Bon-Air Street Railway Company; Cedar Avenue Street Railway Company; East McKeesport Street Railway Company; Glenwood and Dravosburg Electric Street Railway Company; The McKeesport and Reynoldton Passenger Railway Company; Mt. Washington Street Railway Company; Mt. Washington Tunnel Company; Pittsburgh, Allegheny, and Manchester Passenger Railway Company; The Pittsburgh, Allegheny and Manchester Traction Company; Pittsburgh and Charleroi Street Railway Company; Pittsburgh and West End Railway Company; Pittsburgh, Canonsburg and Washington Railway Company; Pittsburgh, Crafton and Mansfield Street



writs of certiorari issue to review the judgments of the United States Circuit Court of Appeals for the Third Circuit entered in the above entitled case.

### **Summary Statement of the Matter Involved.**

Since 1902, Pittsburgh Railways Company, debtor, has been in possession of and has occupied, used and held properties of approximately fifty-five street railway companies (hereinafter referred to as "underliers"), which properties, in conjunction with its own properties, the debtor has operated as a unified street railway transportation system in and about the City of Pittsburgh, Pennsylvania, the system being known as the Pittsburgh Railways System (R. 8, 9, 55, 83). The underliers' properties were in possession of the debtor under certain leases and operating agreements which require the debtor to pay expenses of operation and ordinary maintenance and all taxes of the underliers (R. 9, 10).

The Pittsburgh Railways System consists of approximately 560 miles of track, incline plane properties, cars and buildings used primarily for the housing of cars. The debtor itself owns 28 miles of track, cars and other

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Railway Company; Pittsburgh, Neville Island and Coraopolis Railway Company; Pittsburgh Union Passenger Railway Company; Second Avenue Passenger Railway Company; Second Avenue Traction Company; The Second Avenue Traction Company; Superior Avenue and Shady Avenue Street Railway Company; United Traction Company of Pittsburgh; Washington and Canonsburg Railway Company; West End Traction Company; West Liberty and Suburban Street Railway Company; West Shore Electric Street Railway Company; Consolidated Traction Company; Ardmore Street Railway Company; Central Passenger Railway Company; The Central Traction Company; Fort Pitt Traction Company; The Pittsburgh Traction Company; The Duquesne Traction Company; The Duquesne Street Railway Company; Federal Street and Pleasant Valley Passenger Railway Company; The Morning-side Electric Street Railway Company; Seventeenth Street Incline Plane Company.

miscellaneous property (R. 108). The debtor has always paid, directly, the expenses of operation and ordinary maintenance and all taxes of the underliers. None of such payments have been made by the underliers (R. 9).

On May 10, 1938, the debtor filed a voluntary petition to effect a plan of reorganization under the provisions of Section 77B of the Bankruptcy Act, and on the same day the court approved the petition as properly filed and continued the debtor in possession with authority to operate its business (R. 1). By order entered June 14, 1938, the court appointed trustees of the debtor and its subsidiary, Pittsburgh Motor Coach Company, and authorized the trustees, *inter alia*, to

"preserve, maintain, manage and operate and keep in good order, condition and repair, the property and estate in possession of and/or owned by the debtor, and to manage and conduct its business; and without limiting the generality of the foregoing, to collect and receive the income, rents, revenues, tolls, issues, and profits of said property and estate; \* \* \* and to pay all taxes and assessments due or to become due upon the property in possession and/or owned by the debtor." (R. 107)

Pursuant to their authority the trustees have since their appointment and qualification been operating the business of both debtor and the subsidiary, using in their operation the properties of the underliers. However, the trustees have neither affirmed nor disaffirmed the leases and operating agreements between the debtor and its underliers.

On March 10, 1939, the trustees of the debtor filed a petition with the District Court praying for instructions with respect to the payment of taxes of the underliers which became due and payable after the approval

*Petition for Writ of Certiorari.*

of the debtor's original petition (May 10, 1938), together with certain other taxes of the debtor and its subsidiary not material herein (R. 8-26). The taxes of the underliers involved are set forth below.\* The trustees' petition averred that at the date of filing the original petition, the cash on hand was \$230,260.00, and on March 8, 1939, was \$1,537,247.46, the latter amount being sufficient to pay all taxes as to which instructions were requested by the trustees (R. 16). None of the underliers had funds with which to pay any of the taxes assessed against them (R. 17).

The trustees' petition was referred to a special master for hearing and a report thereon (R. 26). At the hearing objections to the payment of the taxes of the underliers were filed by the Tort Creditors' Committee of the debtor (R. 28). Mr. Fitzgerald, one of the trustees who has been in active charge of the operation of the Pittsburgh Railways System since 1924, testified at the hearing that (a) since it was created in 1902 there has been absolutely no effort to account for reve-

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* Unpaid balances of Federal income taxes for the year 1937, payments due June 15, September 15, and December 15, 1938	\$ 97,412.14
Federal income taxes for the year 1937, withheld at source in respect to interest upon obligations of underliers, payment due June 15, 1938	6,850.01
Pennsylvania corporate net income taxes for the year 1937, payment due May 15, 1938	27,639.59
Federal income taxes for the year 1938	50,501.26
Federal income taxes for the year 1938, withheld at source with respect to interest upon the obligations of underliers	2,668.08
Pennsylvania corporate net income taxes for the year 1938	18,335.72
Pennsylvania capital stock taxes for the year 1938	64,294.57
Pennsylvania corporate loans taxes for the year 1938 in respect to interest upon the obligations of underliers	17,502.56
<b>Total</b>	<b>\$285,203.93</b>

nues and operating expenses of individual underliers; (b) to attempt to account for revenues and operating expenses of individual underliers would be tremendously expensive, and the results would not furnish a dependable basis for allocating revenues; (c) the only way in which net earnings of each underlier could be determined would be to operate each individually, such individual operation being physically impossible and unsatisfactory to the public and to municipal and state authorities; and (d) at present he knows of no method of determining what relative rentals should be paid to the various underlying companies whose properties have been utilized by the debtor or its trustees since May 10, 1938 (R. 54, 55, 57). Mr. George, one of the trustees charged with the duty of preparing a plan of reorganization, testified that (a) he believes there will not be a great amount of abandonment of properties of the underliers in the reorganization; (b) he did not consider it practicable for the trustees to say what properties of the underliers will or will not be embraced in the contemplated plan of reorganization; and (c) the properties of the underliers whose taxes were being considered are presently being operated by the trustees (R. 60-62).

The special master filed a report recommending, *inter alia*, that the taxes of the underliers should not be paid by the trustees (R. 89, 90). Exceptions were filed to the special master's report by Philadelphia Company (petitioner herein and principal creditor of and owner of all the capital stock of the debtor), and by certain underliers (R. 97-106). An argument on the exceptions of your petitioners herein was held before the District Court and, subsequent thereto, counsel for the trustees filed a statement with the District Court recommending the payment of all taxes of the underliers, except Federal income taxes in so far as such income taxes were produced by payments made to the underliers by Philadelphia Company in discharge of its obligations

as guarantor of the underliers' lease covenants and except Pennsylvania corporate net income taxes unless and until the liability of the underliers for such taxes should be determined (R. 129-140).

The District Court entered its opinion and order holding and directing that the underliers' taxes be paid to the extent recommended by counsel for the trustees (R. 107-116). From said order of the District Court, in so far as it directed payment of the underliers' taxes, the Tort Creditors' Committee and the City of Pittsburgh appealed to the Circuit Court of Appeals for the Third Circuit (R. 117-119). The appeals were heard together, and in its opinion filed April 30, 1940, the Circuit Court of Appeals reversed the District Court (R. 146-152). The orders of the Circuit Court entered April 30, 1940 (R. 152) were vacated and amended orders entered June 12, 1940 (R. 154, 155), in which it was directed that the order of the District Court be reversed in so far as it directed the payment of taxes involved in the appeals.

#### **Jurisdiction.**

The Circuit Court of Appeals entered its orders on April 30, 1940 (R. 152). On June 12, 1940, said orders were vacated (R. 153, 154), and amended orders were entered (R. 154, 155). No petition for rehearing was filed. The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925, Chap. 229, § 1, 28 U. S. C. A. § 347, since this is a cause in which final orders of a Circuit Court of Appeals have been entered.

#### **Question Presented.**

Where the trustees of a street railway company in reorganization under Section 77B and Chapter X of the



Bankruptcy Act are operating the business of the debtor, using the property of the debtor and properties of lessor or underlying street railway companies (comprising approximately 95% of the system's trackage) which properties have been operated as a unified system by the debtor since 1902 pursuant to leases and operating agreements requiring the payment by the debtor of all taxes assessed against such underlying companies, and the trustees take possession of, occupy and use the properties of the underlying companies, receive all revenues therefrom and use such revenues as a common fund with which to pay all operating charges of the system, such as wages, cost of supplies, repairs and improvements to the properties of the debtor and the underliers, insurance premiums, and for the purchase of new equipment, for a period of over two years without either affirming or disaffirming the leases and operating agreements, should the trustees be authorized and directed to pay the taxes legally levied against the underlying street railway companies which became due and payable, or which accrued, after the approval of the debtor's original petition, when the trustees are possessed of ample funds derived almost entirely from the use of said underlying companies' properties and none of the underliers have funds with which to pay any of said taxes?

**Reasons Relied on for Allowance of the Writs.**

1. The decision of the court below is in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *Webster & Atlas National Bank of Boston v. Palmer, et al.*, 111 Fed. (2d) 215, decided April 16, 1940, in which the court directed the trustees of the debtor to pay all taxes legally assessed by state and local authorities against the debtor's underliers so long as operation of the underliers' properties continued by the debtor's trustees. A petition for writ of certiorari

in the *Webster & Atlas* case was filed with this court on June 1, 1940.

2. In holding that the trustees of the debtor may not make payment of the underliers' taxes which became due and payable, or which accrued, after the approval of the debtor's original petition for reorganization, the Circuit Court of Appeals decided important questions of Federal law which have not been, but should be, settled by this court.

(a) The decision of the court below raises an important question with respect to the duty of trustees appointed under the Bankruptcy Act to pay taxes assessed against the business of a lessor or underlier of the debtor when such business is operated by the debtor's trustees pending the affirmance or disaffirmance of the lease. In no case has this court determined that question.

(b) The decision of the court below raises an important question as to the interpretation of the Act of June 18, 1934, 48 Stat. 993 (28 U. S. C. A. § 124a) which directs that any trustee appointed by any United States court who is authorized by said court to conduct any business shall be subject to all state and local taxes applicable to such business. Under the decision of the Circuit Court of Appeals, this Act would not be applicable to the taxes of a lessor or underlying company whose business was being conducted by the trustees of the debtor under authority of an order of the court.

(c) As so construed by the Circuit Court of Appeals there is a serious question whether this Act, in the light of the power of the debtor's trustees to retain possession of leased property until rejected by them, does not contravene the Fifth Amendment to the Constitution of the United States.



WHEREFORE your petitioners respectfully pray that writs of certiorari be issued out of and under the seal of this Honorable Court to the Circuit Court of Appeals for the Third Circuit, commanding that court to certify and send to this court, for its review and determination on a day certain to be therein named, a full and complete transcript of the record and all proceedings in this case; that the orders of the Circuit Court of Appeals for the Third Circuit may be reversed; and that your petitioners may have such other and further relief in the premises as to your Honorable Court may seem meet and just.

And your petitioners will ever pray, etc.

PHILIP A. FLEGER,  
W. A. SEIFERT,

*Attorneys for Philadelphia Com-  
pany and Certain Underliers,  
Petitioners.*

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**BRIEF IN SUPPORT OF PETITION FOR  
CERTIORARI.****I.****Opinions Below.**

The opinion of the District Court (McVicar, J.) has not yet been officially reported; it appears at pages 107 to 113 of the record. The opinion of the Circuit Court of Appeals (Maris, C. J.) is reported in 111 Fed. (2d) 932, and will be found at pages 146 to 152 of the record.

**II.****Jurisdiction.**

A statement of the grounds on which the jurisdiction of this court is invoked is contained in the petition.

**III.****Statute Involved.**

Act of June 18, 1934, 48 Stat. 993 (28 U. S. C. A., Sec. 124a):

"Sec. 124a. STATE TAXATION: BUSINESS CONDUCTED BY RECEIVERS, TRUSTEES OR OTHER COURT OFFICERS SUBJECT TO

"Any receiver, liquidator, referee, trustee, or other officers or agents appointed by any United States court who is authorized by said court to conduct any business, or who does conduct any business, shall, from and after June 18, 1934, be subject to all State and local taxes applicable to such business the same as if such business were conducted by an individual or corporation: *Provided, however,* That nothing in this section contained shall be construed to prohibit or prejudice the collection of any such

taxes which accrued prior to June 18, 1934, in the event that the United States court having final jurisdiction of the subject matter under existing law should adjudge and decide that the imposition of such taxes was a valid exercise of the taxing power by the State or States, or by the civil subdivisions of the State or States imposing the same."

**IV.**

**Statement of the Case.**

A statement of the essential facts of the case is included in the petition.

**V.**

**Specification of Errors Intended to Be Raised.**

The Circuit Court of Appeals erred:

1. In reversing the order of the District Court.
2. In holding that the taxes of the underliers which became due and payable after the approval of the debtor's original petition should not be paid by the trustees of the debtor.
3. In holding that the taxes of the underliers which accrued after the approval of the debtor's original petition should not be paid by the trustees of the debtor.
4. In requiring payment, in violation of the Fifth Amendment to the Constitution of the United States, of the debtor's taxes out of funds in the possession of the trustees derived largely from the operation of the underliers' properties while forbidding any payment of the underliers' taxes from those funds.

5. In holding that the court must first determine the property of the underliers which is being used, the extent of its use and the net earnings being derived from it or its value before any payment to the underliers on account of use and occupation can be permitted.

6. In holding that the only obligation of the debtor or of the trustees to pay taxes of the underliers is by virtue of covenants in the leases and operating agreements under which the debtor was in possession of the properties of the underliers.

7. In failing to treat the taxes of underliers as operating expenses entitled to payment as expenses of administration.

8. By failing to give proper effect to the Act of June 18, 1934, 48 Stat. 993 (28 U. S. C. A., Sec. 124a).

## VI.

### Argument.

1. The decision of the court below is in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *Webster & Atlas National Bank of Boston v. Palmer et al.*, 111 Fed. (2d) 215, decided April 16, 1940.

In the instant case the Circuit Court of Appeals held that the trustees of the debtor should not use funds in the estate of the debtor for payment of taxes of the underliers whose properties are being operated by the trustees of the debtor, together with the debtor's property, as a unified system. In the *Webster & Atlas* case the court directed the trustees of the debtor to pay all taxes legally assessed by state and local authorities against the debtor's underliers so long as operation of

the underliers' properties continued by the debtor's trustees.

In the *Webster & Atlas* case the trustees in reorganization of the New York, New Haven & Hartford Railroad Company rejected the leases of certain underlying lessor companies. The underliers being unequipped for independent operation, the District Court, pursuant to Section 77(c)(6) of the Bankruptcy Act, ordered the New Haven's trustees to continue operation of the underliers' properties. Under a segregation formula, accepted by the District Court, it appeared that the underliers' lines were operated at a loss, and it appeared, the Circuit Court so recognizing, that the continued diversion of funds from the New Haven's estate to meet these deficits of the underliers would jeopardize the New Haven's own creditors. Accordingly, the New Haven's trustees filed a petition asking for authority to withhold the further payment of taxes of the underliers. The Circuit Court of Appeals held that the Act of June 18, 1934, 48 Stat. 993 (28 U. S. C. A., Sec. 124a) hereinafter referred to as "Sec. 124a", required the New Haven's trustees to pay the underliers' taxes so long as they operated the underliers' properties, saying:

"28 U. S. C. A. § 124a, enacted in 1934, declares that 'Any receiver, liquidator, referee, trustee, or other officers or agents appointed by any United States court who is authorized by said court to conduct any business, or who does conduct any business, shall, from and after June 18, 1934, be subject to all State and local taxes applicable to such business the same as if such business were conducted by an individual or corporation \* \* \*'. This section was applied generally, even against the bankruptcy trustee's claim of lack of funds, in *Ingels v. Boteler*, 9 Cir., 100 F. 2d 915, affirmed 308 U. S. 57, 60 S. Ct. 29, 84 L. Ed. . . . . And it was held applicable to a

railroad's trustee under § 77. *Thompson v. Louisiana*, 8 Cir., 98 F. 2d 108, 111.

"The district court held, however, that even if this statute ordinarily applied to railroad trustees, yet it did not apply when such officers were operating only for account of a lessor road under § 77, sub. c (6). But we believe that, since that statute has placed the duty of operation upon the lessee, the lessee's trustees are thereby made 'agents of the court' within the meaning of 28 U. S. C. A. § 124a. The Old Colony and the Boston and Providence, were they operating their lines, would have to pay their share of the taxes levied against the Boston Terminal Company. Section 25 of the Massachusetts statute of 1896 makes them directly liable to the tax collector for the real estate taxes, and their duty under § 10 of the same Act to pay all other taxes to the Terminal Company could be enforced directly by the taxing authorities. Now by law the duties of operation have devolved upon the New Haven, as lessee, and upon the New Haven trustees. If there existed sufficient moneys of the Old Colony and the Boston and Providence, no one could gainsay the duty of the New Haven trustees to apply those moneys to payment of the taxes. In accordance with the view we have expressed above—that operation must continue until abandonment has been legally ordered, even though the New Haven trustees must go for funds to the New Haven estate—we conclude that under 28 U. S. C. A. § 124a taxes legally assessed by state and local authorities must be paid by the New Haven trustees while operation continues." 111 Fed. (2d) 219, 220. (Italics supplied)

In the instant case, the Circuit Court of Appeals, in holding that the trustees of the debtor should not pay the taxes of the underliers, stated as its reasons therefor



that (a) the taxes in question are taxes of the underliers, not of the debtor, and are owing by the debtor only as a contractual obligation under the leases and operating agreements and then only if the trustees affirm the leases and operating agreements; (b) the trustees are not trustees of the underliers; (c) payment of the taxes is not immediately necessary to prevent harmful action by the taxing authorities against the properties of the underliers; and (d) payment of these taxes cannot be justified as a partial allowance for use and occupancy prior to affirmance or rejection of the leases and operating agreements unless it is first determined what is a fair allowance on the basis of revenues derived from or of the fair value of the property of the underliers being used, since otherwise, to the extent that the amount paid as taxes exceeded sums justly due for use and occupation, funds of the debtor would be diverted to the preference of the underliers over the creditors of the debtor.

The same situation, in effect, existed in the *Webster & Atlas* case, i. e., (a) the taxes were those of the underliers, not of the debtor; (b) the trustees of the New Haven were not, as such, trustees of the underliers; (c) the reorganization court could hold off the tax gatherers and thus payment was not immediately necessary to continued operation of the underliers' properties; and (d) the underliers admittedly were operating at a loss and their property was of no value to the New Haven, with the result that the payment of their taxes by the New Haven's trustees diverted funds to the underliers' account to the prejudice of the creditors of the debtor and no attempt was made to justify the payment of the underliers' taxes as an allowance for use and occupation. Nevertheless, the Circuit Court of Appeals for the Second Circuit held that the New Haven's trustees were agents of the court within the meaning of



Sec. 124a and as such were subject to all state and local taxes applicable to the business conducted by them, including the underliers' taxes, so long as they operated the underliers' properties.

Thus, in all essential respects, the situation in this and in the *Webster & Atlas* case are the same. Yet opposite results were reached by the Circuit Courts.

It may be thought or asserted that the *Webster & Atlas* case can be distinguished from this case on the ground that the New Haven was in reorganization under Section 77 of the Bankruptcy Act relating to railroad reorganizations, and the continued operation of the underliers' properties by the New Haven trustees was required under subsection (c) (6) thereof, which provides:

"(6) If a lease of a line of railroad is rejected, and if the lessee, with the approval of the judge, shall elect no longer to operate the leased line, it shall be the duty of the lessor at the end of a period to be fixed by the judge to begin the operation of such line, unless the judge, upon the petition of the lessor, shall decree after hearing that it would be impracticable and contrary to the public interest for the lessor to operate the said line, in which event it shall be the duty of the lessee to continue operation on or for the account of the lessor until the abandonment of such line is authorized by the Commission in accordance with the provisions of section 1 of the Interstate Commerce Act as amended."

However, this distinction relates only to the compelling reason for the continued operation of the underliers' properties. In the New Haven reorganization such continued operation was required by appropriate orders of the court under Section 77(c) (6) of the Bankruptcy Act which authorizes the entry of such an order where

separate operation would be impracticable and contrary to the public interest. In the instant proceedings, operation of the underliers' properties, in conjunction with the debtor's properties, as a unified system is continued under the practical compulsion that separate operation of the underliers' properties is impossible and, even if possible, would be impracticable and unsatisfactory to the public and municipal and state authorities (R. 55), although there is no applicable provision of the Bankruptcy Act authorizing the court to enforce, by its order, this practical necessity of unified operation.

Whatever the reason for the operation of the underliers' properties by the debtor's trustees, the point is that in the New Haven case the court held that under Sec. 124a the trustees must pay the underliers' taxes while operation of the properties continues, and in the Pittsburgh Railways case the court held they may not. The Circuit Court of Appeals for the Second Circuit in the *Webster & Atlas* case clearly points out that it is the continued operation which requires the payment of the taxes irrespective of the reason for that continued operation, saying:

"It is contended, however, that both the taxes and the interest are 'operating expenses,' as the Massachusetts statute provides. But it is not necessary to pass on whether either type of payment is an operating expense, nor need we decide whether § 77, sub. c (6), in and of itself, requires the lessee to pay such expenses not indispensable to the continuance of railroad operations. Whatever the answer to these perplexing questions, federal statutes [i. e., Sec. 124a and Sec. 124—insert ours] impose upon the New Haven trustees a direct duty to meet both the tax and the interest charges." (P. 219)

2. In holding that the trustees of the debtor may not make payment of the underliers' taxes which became due and payable, or which accrued, after the approval of the debtor's original petition for reorganization, the Circuit Court of Appeals decided important questions of Federal law which have not been, but should be, settled by this court.

(a) THE DECISION OF THE COURT BELOW RAISES AN IMPORTANT QUESTION WITH RESPECT TO THE EXTENT OF THE DUTY OF TRUSTEES APPOINTED UNDER THE BANKRUPTCY ACT TO PAY TAXES ASSESSED AGAINST THE BUSINESS OPERATED BY THEM.

In all cases decided by this court and by the lower Federal courts relating to the payment of taxes by trustees or receivers, it has been held that it is their duty to pay all taxes applicable to the business conducted, as if such business were conducted by an individual or corporation; and such taxes have been accorded priority whether or not they are a lien upon the property of the debtor. *Michigan v. Michigan Trust Co.*, 286 U. S. 334, 76 L. Ed. 1136; *Boteler v. Ingels*, 308 U. S. 57, 84 L. Ed. 20; *Coy v. Title Guarantee & Trust Co.*, 220 Fed. 90; *Bear River Paper & Bag Co. v. City of Petoskey et al.*, 241 Fed. 53; *MacGregor v. Johnson-Cowdin-Emmerich, Inc.*, 39 Fed. (2d) 574; *Hardee et al. v. American Security & Trust Co.*, 77 Fed. (2d) 382. However, in all of these cases the taxes in question were the taxes of the debtor or bankrupt corporation itself. In no case has this court decided whether this rule should not be applied as well to taxes levied against underliers so long as the business of such underliers is being operated by the debtor's trustees in conjunction with the debtor's business.

In the present case, the street railway properties used and operated by the trustees have been operated since 1902 as a unified system, and all of the revenues therefrom have been kept in a single fund without at-

tempting to account for the revenues or earnings of the various companies comprising the system. There is no dependable basis for allocating revenues. This could be determined only by operating each underlier separately, which is a physical impossibility. The properties operated in the unified system consist almost entirely of the properties of the underliers, and the funds in the hands of the trustees represent, for all practical purposes, the earnings of the trustees from the use and operation of the underliers' properties. It is expected that the system will be reorganized as a unit and that there will not be any great amount of abandonment of properties of underlying companies. Under such circumstances, the District Court held that the rule laid down in the above authorities should be applied to this case, thus requiring the trustees to pay out of the earnings of the unified system, all taxes of the underliers incurred as a result of the operation of their properties by the trustees pursuant to the order of the District Court entered June 14, 1938. The Circuit Court of Appeals held otherwise, refusing to permit payment of the underliers' taxes on the ground that such payments could not be justified either as tax obligations of the debtor itself, or, in the absence of a precise ascertainment of the revenues derived from or fair value of each separate underlier's property (an admittedly impossible task), as payments on account of use and occupation of the underliers' properties.

It is submitted that the decision of the District Court was correct and that the Circuit Court of Appeals erred in reversing that decision. Having taken possession of the underliers' properties, the trustees should be required to take them *cum onere*, and the taxes here in question arising as a result of the operation of the properties of the underliers should be held as much a part of the trustees' expenses as current upkeep. As stated

by the special master appointed by the District Court to report upon the trustees' petition with respect to the payment of the underliers' taxes:

"It can hardly be doubted that the separate operation of many of the properties of the several owners would be impracticable. Although the underlying companies themselves are not in bankruptcy or reorganization, their properties in reality are in reorganization to the extent that they are in the possession of the trustees, will probably be involved somehow in the reorganization of Pittsburgh Railways Company if any reorganization is effected, and are being operated." (R. 87, 88)

Taxes are intensely practical. In substance, all of the properties in the possession of the trustees are in reorganization and must be given the same consideration as the properties of the debtor for the purpose of working out a reorganization, for which reason it is necessary that all taxes be paid.

Whether the well established principle that a receiver or trustee is under a duty to pay all taxes accruing as a result of the continued operation of the debtor's business shall be applied to taxes of underliers whose business is also operated by such trustees, is an important question as to the duties of trustees appointed under the Bankruptcy Act which has never been, but should be, determined by this court.

(b) THE DECISION OF THE COURT BELOW RAISES AN IMPORTANT QUESTION AS TO THE INTERPRETATION OF SEC. 124a.

Sec. 124a directs that any trustee appointed by any United States court who is authorized by said court to conduct any business shall be subject to all state and local taxes applicable to such business. In the *Webster*



& *Atlas* case, *supra*, it was held that under this Act, so long as the trustees of the debtor operate the underliers' properties pursuant to court order, they must pay the taxes of such underliers.

By order of the District Court, entered June 14, 1938, the trustees of Pittsburgh Railways Company were authorized, *inter alia*, to "\* \* \* operate \* \* \* the property and estate in possession of and/or owned by the debtor." The trustees are operating the business of the underliers under authority of this order. Nevertheless, the court below, without any reference to Sec. 124a, the applicability of which was urged upon it, held that the trustees should not pay state taxes of the underliers despite ample funds in the trustees' hands derived largely from the operation of the business of the underliers.

The effect of the Circuit Court's decision is to confine the application of Sec. 124a to taxes assessed in respect of the business of the particular debtor corporation although the order of court appointing the trustees may authorize or direct such trustees to continue the operation of the business of other corporations previously operated by the debtor under lease or other operating agreement, and has the effect of exempting the trustees from the payment of any Federal, state or local taxes assessed in respect of the business of such other corporations, the business of which other corporations has been operated by the debtor, in conjunction with its own, as a unified transportation system for over thirty years. The differing views of the Circuit Court of Appeals for the Second and Third Circuits raise an important question as to the interpretation of Sec. 124a which has not been, but should be, determined by the decision of this court.

(c) THE DECISION OF THE COURT BELOW LIMITING, AS IT DOES, THE EFFECT OF SEC. 124a RAISES SERIOUS CONSTITUTIONAL QUESTIONS WHICH SHOULD BE DECIDED BY THIS COURT.

The trustees have retained the properties of the underliers for more than two years without taking any steps to affirm or disaffirm the leases and operating agreements. In fact the trustees expect that any reorganization effected will be a reorganization of the system as a unit with very little abandonment of properties. It is essential to any reorganization that most, if not all, properties of the underliers be continued in operation as a unified system. The properties of the debtor are negligible in relation to the entire system, and funds in the hands of the trustees, which increased from \$230,260.00 at the date of the debtor's original petition to \$1,537,247.46 at the date of filing the trustees' petition for instructions as to payment of taxes, are derived almost entirely from the operation of the underliers' properties. Except to the extent that these funds are used for the payment of taxes and other operating and administrative expenses, it is apparent that, since they represent chiefly the revenues of underliers' properties, they are subject to the prior claims of the underliers either in payment of rental under the leases and operating agreements, if affirmed, or for use and occupation, if rejected. As said *In re Schulte Retail Stores Corporation*, 22 Fed. Supp. 612, 615:

"\* \* \* If the lease were affirmed, the liability would be considered as one for rent; if the lease were rejected, the liability would be for use and occupancy, viz., the reasonable value of the use of the premises which, in turn, would probably be the rent specified in the lease. *Irrespective of the legal characteristics of the liability, it would be recognized as an expense of reorganization and, as such,*



*it would enjoy priority over claims that accrued prior to the inception of these proceedings."* (Italics ours)

In such a case, where the debtor's trustees continue to retain possession of and to operate the underliers' properties and to collect and receive the income and revenues thereof, if Sec. 124a be construed, in the light of the power of the trustees to retain possession of leased property until rejected by them, as requiring application of these revenues to the payment of the debtor's taxes but not to the payment of the taxes of the underliers whose properties are retained in possession of the debtor's trustees and operated by them to the benefit of the debtor's creditors, and which taxes of the underliers accrue as the result of such continued operation of their properties by the debtor's trustees, there is a serious question as to whether Sec. 124a, as so construed, does not contravene the Fifth Amendment to the Constitution of the United States which forbids Congress to deprive any person of life, liberty or property without due process of law or to take private property for public use without just compensation.

This court has held that in order that legislation shall not offend against the Fifth Amendment it is necessary that

"the law shall not be unreasonable, arbitrary or capricious, and that the means selected shall have a real and substantial relation to the object sought to be obtained." *Nebbia v. New York*, 291 U. S. 502, 525; *Railroad Retirement Board v. Alton R. Co.*, 295 U. S. 330, 348.

The effect of the decision of the court below is that the properties of the underliers can be retained by the trustees and operated by them for the benefit of the

unified system, including other creditors of the debtor corporation, without any corresponding duty being imposed upon the trustees under Section 124a to pay the taxes of the underliers accruing as a result of such continued operation of their properties. It is submitted that this decision of the court below raises a serious question whether the Acts referred to, as so construed, are not unreasonable, arbitrary and capricious and deprive the underliers of their properties without due process of law.

### **Conclusion.**

Because of the conflict existing between the decision of the court below in this case and the decision of the Circuit Court of Appeals for the Second Circuit in the case of *Webster & Atlas National Bank of Boston v. Palmer et al.*, 111 Fed. (2d) 215, and because the decision of the court below raises important questions of Federal law as to the application, interpretation and constitutionality of Sec. 124a, which questions have never been, but should be, passed upon by this court, it is respectfully submitted that this petition for writs of certiorari should be granted.

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W. A. SEIFERT,

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pany and Certain Underliers,  
Petitioners.*

We, the undersigned, join in and adopt the foregoing Petition and Brief in behalf of the Citizens Traction Company, Penn Street Railway Company and The

Suburban Rapid Transit Street Railway Company,  
underliers of the Pittsburgh Railways Company.

LEE C. BEATTY,  
RICHARD W. AHLERS,

*Attorneys for said Underliers.*

I, the undersigned, join in and adopt the foregoing  
Petition and Brief in behalf of the Allegheny Traction  
Company and Millvale, Etna & Sharpsburg Street Rail-  
way Company, underliers of the Pittsburgh Railways  
Company.

HILL BURGWIN,

*Attorney for said Underliers.*

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